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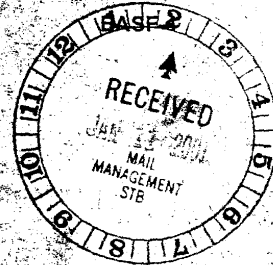
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BASF Corporation

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Public Record



BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Ex Parte No. 582 (Sub No. 1)
MAJOR RAIL CONSOLIDATION PROCEDURES

COMMENTS OF BASF CORPORATION

And

Verified Statement of

TOM O'CONNOR

Snavely King Majoros O'Connor & Lee, Inc.
1220 L St. NW
Washington, DC 20005

Dated: January 11, 2001

January 11, 2001

Ex Parte No. 582 (Sub-No. 1)

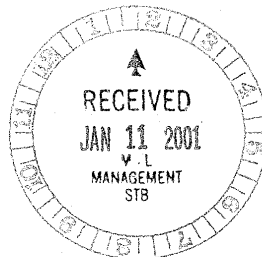
SK Snavely King Majoros O'Connor & Lee
Economic and Management Consultants

BASF-4

201264

January 11, 2001

Mr. Vernon Williams
Secretary
Surface Transportation Board
1925 K St. NW
Washington, D.C. 20423-0001



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Office of the Secretary

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Via Hand Delivery

Dear Mr. Williams:

In response to the Notice of Proposed Rulemaking (NPR) issued by the Surface Transportation Board (STB) on October 3, 2000 in Ex Parte 582 (Sub-No.1), Major Rail Consolidation Procedures, enclosed are the Rebuttal Comments of BASF and supporting Verified Statement of Tom O'Connor.

We have provided the original and 25 copies of the filing, as well as an electronic version in WordPerfect 7.0.

We would appreciate it if your staff would date stamp the second copy of this letter for return to us. Should questions arise, please call me at (202) 371-9149.

Thank you.

Sincerely,

Tom O'Connor

Tom O'Connor
Vice President

January 11, 2001

Ex Parte No. 582 (Sub-No. 1)

BASF Corporation

BASF-4

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**BEFORE THE
SURFACE TRANSPORTATION BOARD**

STB Ex Parte No. 582 (Sub No. 1)

MAJOR RAIL CONSOLIDATION PROCEDURES

COMMENTS OF BASF Corporation

BASF Corporation, by Counsel, respectfully submits these comments in response to the Surface Transportation Board's (Board or STB) Notice of Proposed Rulemaking (NPR), served October 3, 2000.

BASF (BASF) is a major shipper by rail, truck, waterway and pipeline in the US and Canada. We account for more than 22,000 rail carload shipments outbound and an additional 10,000 rail carload shipments inbound annually.

Our approach to transportation and logistics is based on Win-Win-Win. We see three winners in BASF logistics:

- BASF customers and suppliers
- BASF
- Our transportation providers connecting BASF with its customers and suppliers

Our supply and distribution capabilities, commercial viability and costs depend on efficient and effective rail carriers. We see this proceeding as a means of strengthening the Supply Chain and benefiting all of its participants.

Regrettably, at this point most of that potential remains unrealized. In the accompanying statement of Tom O'Connor, we identify the most critical areas in need of improvement and develop specific recommendations to achieve those badly needed improvements in the rail merger process.

The needed improvements can be summarized succinctly:

1. The STB should implement pro-competitive modifications:

- Reciprocal Switching
- Competitive Line Rates
- Bottleneck rate challenges
- Trackage Rights
- Haulage rights

2. The STB should adopt a rebuttable presumption that further mergers are against the public interest.

3. The STB should apply comprehensive and rigorous pre-merger testing within a merger review process segmented into three sequential steps:

- (1) Corporate Merger
- (2) Business Merger
- (3) Operational Merger

4. The STB should guarantee shipper compensation for reduction and loss of rail service attributable to mergers.

5. A Blue Ribbon Advisory Panel should be created to provide timely and objective oversight during merger review and implementation.

The STB needs to leave its passive mode and adopt a proactive pre-merger approach to identifying and solving problems. The STB must realize that the next mergers will involve coast-to-coast operations and more complex systems. Without comprehensive and rigorous pre-merger testing and step-wise integration of systems, the problems will be larger in scope than any mergers experienced to date and will act as an economic brake on all of North America.

While, as previously presented, the NPR has numerous deficiencies, the key areas identified by BASF as most in need of improvement are:

- **The Critical Need for Enhanced Competition**
 - **Open Gateways**
 - **Challengeable Bottleneck Rates**
- **Implementation Plan and Merger Oversight**

In each of these areas the need for an effective remedy is clear. The numerous respondents supporting changes similar to those recommended by BASF reinforce the clarity of the need. Exhibit A to Mr. O'Connor's Verified Statement summarizes the widespread support for change in these key areas.

The remedies presented by BASF can help reverse the debilitating rail performance trends associated with recent mergers and benefit all parties having an interest in rail transportation: they should be adopted by the Board.

In summary these remedies include:

- **Solutions that implement the STB decision to enhance competition**
- **Comprehensive and rigorous pre-merger testing applied in a step-wise process**
- **An expanded role for short lines in solving service problems**
- **Procedures to prevent and recover economic losses caused by service failures**
- **Creation of an empowered Blue Ribbon Advisory Panel to assist in rail mergers**

In 1887, the Interstate Commerce Act was enacted in response to widespread monopolistic activity by the railroads. Now with an increasingly concentrated rail industry it will be only the regulations implemented by the STB as a result of these proceedings that will prevent anti-competitive activity by the anticipated rail duopoly.

If the STB fails to act now, many contend history is bound to repeat itself and the shippers, their customers, the public and the economy will endure a replay of the disruptions associated with prior mergers and bear the burdens associated with uncontrolled monopolistic activities. This may continue until legislation is again enacted to level the playing field.

It seems that there is now a fortuitous confluence of events offering the railroads and the STB the opportunity to promote and adopt fair and practical solutions, without the threat of service disruptions or degradation while giving shippers reasonable assurances of a continuing "competitive" marketplace for rail services. If the railroads and the STB take this opportunity all interested parties can win and benefit in both the short term and the long term. This would avoid the regrettable and unnecessary return to the draconian solutions of earlier times.

The need for such change is effectively summarized in a recent letter to Congress signed by more than 270 industry leaders representing virtually every sector of the US economy.

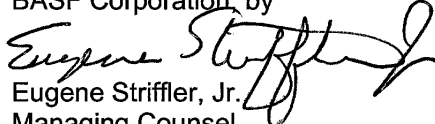
The following excerpt from that letter, which appeared as Exhibit A in our November 17th filing, states the issues clearly:

"...The Staggers Rail Act was enacted in 1980 with the goal of replacing government regulation of the railroads with competitive market forces. Since that time, the structure of the nation's rail industry has changed dramatically. Where there were 30 Class I railroad systems operating in the U.S. in 1979, now there are only seven. While major railroads in North America appear poised to begin another round of consolidations in the near future, the Surface Transportation Board continues to adhere to policies that hamper rail competition. Structural changes in the rail industry combined with STB policies have stopped the goal of the Staggers Rail Act dead in its tracks.

We depend on rail transportation for the cost-effective, efficient movement of raw materials and products. The quality and cost of rail transportation directly affects our ability to compete in a global marketplace, generate low cost energy, and contribute to the economic prosperity of this nation. Current rail policies frustrate these objectives by allowing railroads to prevent competitive access to terminals, maintain monopolies through "bottleneck pricing," and hamper the growth of viable short line and regional railroads through 'paper barriers'..."

BASF has been paying increasing prices for decreasing service, as well as paying in many other ways for a deteriorating rail system. The remedies developed by BASF in this series of filings can help reverse these debilitating rail performance trends and should be adopted by the Board.

Respectfully Submitted
BASF Corporation, by



Eugene Striffler, Jr.
Managing Counsel
3000 Continental Drive, North
Mt. Olive, NJ 07828-1234

BASF Corporation

BASF-4

Before the Surface Transportation Board

**Rebuttal Comments in Response to
Notice of Proposed Rulemaking**

In

**STB Ex Parte No. 582 (Sub-No. 1)
Major Rail Consolidation Procedures**

Filed on Behalf of

BASF Corporation

VERIFIED STATEMENT OF

Tom O'Connor

**Vice President
Snively King Majoros O'Connor & Lee, Inc.
1220 L St NW
Washington DC 20005**

January 11, 2001

Ex Parte No. 582 (Sub-No. 1)

TABLE OF CONTENTS

A. INTRODUCTION	1
B. SUMMARY	1
C. ANALYSIS	2
I. The STB Should Adopt a Rebuttable Presumption that Further Class I Rail Mergers Are Contrary to the Public Interest.	2
II. An Advisory Panel Should Be Established To Provide Objective Assistance in Merger Review and Implementation.	4
III. The STB Should Segment the Merger Review Process into Three Sequential Phases.	5
Step 1 - The Corporate Merger	5
Step 2 - The Business Merger	5
Step 3 - The Operational Merger	5
IV. The STB Should Address Merger-Related Service Failures Proactively.	8
V. The Board Should Not Only Protect Competition, It Should Enhance It.	12
Preserving Competition	13
Enhancing Competition	13
D. CONCLUSION	16
Exhibit A: Summary of Recommendations of Other Parties	18

A. Introduction

My name is Tom O'Connor. I am Vice President of the economic and management consulting firm of Snavelly King Majoros O'Connor & Lee, Inc. I have served as an economist with the Interstate Commerce Commission (ICC), the United States Railway Association (USRA), Conrail, the Association of American Railroads (AAR) and two consulting firms, including my present firm. A summary of my qualifications is attached.

BASF retained my firm to review the record of this proceeding and to analyze the Surface Transportation Board's (Board or STB) present and prospective role in the impending consolidation of the railroad industry.

We have developed, in collaboration with BASF, recommendations on rule revisions designed to retain and enhance existing rail competition while avoiding the service disruptions that have characterized recent rail mergers. Over the past six months, working with BASF, we have presented and supported those recommendations in four successive stages of this proceeding:

- May 16, 2000 Opening Statement, (BASF-1)
- June 5, 2000 Reply Statement, (BASF-2)
- November 17, 2000 Comments on the Notice of Proposed Rulemaking, (BASF-3)
- This January 11, 2001 Rebuttal Statement (BASF-4)

B. Summary

As BASF stated in its previous comments filed in this proceeding, the policy statements in the Notice of Proposed Rulemaking (NPR) show promise that the Board is recognizing the weaknesses of its past merger reviews. However, additional policy changes are advisable and the implementation procedures remain largely undefined.

The comments by the parties to this proceeding widely recognize the need for fundamental change in the Board's policies toward rail competition in general, and rail mergers in particular.

A summary of such responses was included as Exhibit B to my November 17 Verified Statement and a similar summary of supporting filings is included as Exhibit A to this statement.

BASF Corporation

BASF-4

BASF, Williams, OxyChem, OxyVinyls and many other parties to this proceeding, including railroads, shippers and governmental agencies, have called for changes including:

- **Enhanced Competition**
- **Open gateways and limited open access**
- **Provisions to allow challenges to bottleneck rates**
- **Service Assurances**

BASF, Williams and other parties also advocate essential changes in the following two areas:

- **Adoption of a three phased merger review and approval process**
- **Greater merger implementation and oversight responsibilities for the Secretary of Transportation, assisted by an Advisory Panel reporting to the Secretary**

Often the presentations in proceedings such as this become overheated and somewhat one-sided. However, too much is at stake to allow parochial views to prevail. Railroads, shippers and the public deserve better, and can have better.

In the remainder of this statement we summarize five areas in which change is essential in order to preserve and enhance the competitive strengths of both railroads and the industries they serve.

C. Analysis

I. The STB Should Adopt a Rebuttable Presumption that Further Class I Rail Mergers Are Contrary to the Public Interest.

The US Department of Agriculture (USDA) has recommended that the Board adopt a "rebuttable presumption" that any further Class I mergers are not in the public interest. The Board policy is in harmony with this position (Section 1180.1) and we strongly agree with the USDA recommendation.

Past mergers were performed in a market with multiple Class I railroads. During the 1980's and early 1990's the public benefits from many of those mergers appeared clear. At that point in time the ICC/STB was correct in adopting a pro-merger stance. The situation is radically different now. There are few remaining Class I railroads. Rail-to-rail competition has all but disappeared in many areas.

The Board, in undertaking this proceeding, has acknowledged that the original guidelines need to be revised to meet current conditions. In its general policy statement, §1180.1, the Board states that it will not favor consolidations that reduce

railroad and other transportation alternatives to shippers unless there are substantial and demonstrable public benefits that cannot otherwise be achieved.

BASF and many other shippers have already seen their rail options decrease from two or more carriers to one. With the remaining mergers expected to be end-to-end, there is little, if any, excess capacity to be wrung from the system. Further mergers will significantly diminish competition without appreciably increasing efficiency. Public benefits from future Class I mergers will be small to non-existent. These mergers will primarily benefit the railroads – often to the detriment of their customers.

The risks to the economy are substantial. Recent merger experience has shown that even what were thought to have been the railroads' best laid plans failed to avert severe and prolonged service disruptions. Given the sheer size of future Class I mergers, the possibility of supply chain gridlock across North America is real. A merger offering little in compensating public benefits could in fact bring the North American economy to a halt.

We see limited potential for public benefits arising from future mergers of Class I railroads under either the existing merger guidelines or the STB-proposed changes. However there is serious risk of the North American transportation network becoming disabled due to such mergers.

Accordingly, BASF recommends that the Board adopt the proposal of the U.S. Department of Agriculture that there be a "rebuttable presumption" that any further mergers will increase concentration and market power and reduce competition. This will not close the door on further mergers. However, it will establish the threshold requirement that the applicants must demonstrate that their merger benefits the public, not just themselves.

Discussion of Alternative Views

The alternative views are somewhat sparse, regarding public benefits. For the most part even the Class 1 railroads are in agreement with the proposed STB policy on this issue. They realize that claims made by the applicants of public benefits accruing from the proposed merger will be under increased scrutiny and will require increased proof that they can be realized. UP stated that, "This is an appropriate way to "raise the bar" for future mergers." (Reply p.20)

The major objections to this rebuttable presumption concept came from BNSF and CP. Those railroads based their arguments, in part, on their belief that the STB now assumes there are no public benefits to be gained from future mergers. This is an erroneous assumption.

We agree, with UP, that the STB has simply "raised the bar" on the burden of proof to the applicants. In past mergers some estimates of the public benefits were unrealistically high and proved unobtainable. The STB has taken a logical step:

requiring the applicant to prove its claims of public benefits. The STB must now complete that step by codifying how that will be done.

BASF reaffirms its agreement with the Board's position and urges a rebuttable presumption regarding inclusion of public benefits. If the public benefit of a merger can not be adequately supported, that merger should not be permitted.

II. An Advisory Panel Should Be Established To Provide Objective Assistance in Merger Review and Implementation.

BASF recommends the creation of an empowered Blue Ribbon Advisory Panel to assist during merger review and implementation. The Advisory Panel should report to the US Secretary of Transportation, assisting the STB by developing objective and impartial recommendations on issues designated by the Secretary. The recommendations of the Advisory Panel should be binding on the STB unless compelling evidence indicates otherwise.

The Advisory Panel would focus on technical issues for which STB resources are insufficient. Examples of areas in which the Panel should assist include:

- review of the railroad operating plans;
- approval of applicant railroad testing plans, processes, and results;
- assistance with measurement of service benchmarks and
- compensatory damages for merger-related service failures.

This panel must be representative and balanced to ensure objectivity and impartiality, and should include railroads and shippers, both large and small, along with government representation. The recommendations of the Advisory Panel should be binding on the STB unless subsequent compelling evidence indicated otherwise.

Discussion of Alternative Views

In its reply, CSX noted their endorsement of an external advisory body, which they referred to as the "Service Council". They further elaborated on the benefits derived from the use of such an organization in the Conrail case, then called the "Transaction Council". We agree with CSX that such an organization would be of great benefit to the STB, the applicants, and all of the other parties affected by the merger process. However, experience in the Conrail case indicates more is needed. The recommended Advisory Panel meets that need.

BASF re-affirms its request that the STB retain and enhance such an advisory organization in its revised regulations. The BASF-recommended Advisory Panel should be a mandatory part of the process in all future mergers.

III. The STB Should Segment the Merger Review Process into Three Sequential Phases.

BASF recommends a three-step merger application process, involving comprehensive and rigorous testing. This application process should consist of:

- 1. Corporate Merger**
- 2. Business Merger**
- 3. Operational Merger**

Step 1 - The Corporate Merger

The primary objective of the Corporate Merger is to determine whether the applicants can establish a prima facie case overcoming the rebuttable presumption against further mergers. The applicants would be required to establish that the proposed merger would yield more in public benefits than it would cost in lost competition. The filing requirements for the Corporate Merger would consist of financial and organizational information, along with the estimation of the downstream effects. Generalized statements of the harm and benefits of the merger and the applicants' plans for overcoming the harms should also be submitted. If the applicants fail this preliminary test of overcoming the rebuttable presumption against future mergers, the matter is put to rest. The merger is rejected, saving the railroads, the STB and the economy in general considerable time and effort.

Step 2 - The Business Merger

The majority of the filing requirements, including the operation integration plans, would fall under the Business Merger application. The Business Merger would include the market study identifying specific competitive harms and the determination of conditions that will resolve those harms in addition to enhancing competition. Shipper and small railroad comment would be inherent in this process. Also during step two a schedule should be developed for the third, or operational, step. This schedule would prescribe the testing programs, the capacity measures, and the detailed operational changes that would be required to make the merging railroads operate as one. The Business Merger step would culminate in approval or disapproval of the merger.

Step 3 - The Operational Merger

Working from the schedule developed in the Business Merger, the Operational Merger would apply the testing programs, capacity measures and detailed operational changes required to make the merging railroads operate as one. Both the railroads and their customers will win from this extensive pre-merger testing and step-wise integration of the applicants systems. Problem areas will be illuminated and workable solutions could be put in place before the "point of no return" has been reached. The tests and measures of the Operational Merger

step should go far towards preventing the chaos experienced in recent Class I mergers.

Discussion of Alternative Views

BNSF and CN opposed the concept of the three-step process proposed by BASF, Williams and others. BNSF's issues focused on (1) the clarity of distinctions between each of the three phases and (2) meeting the statutory or regulatory deadline.

BNSF feared that delays in concluding the process could have the effect of creating uncertainty in the financial markets, which are vital to the merging systems. The process proposed by BASF was characterized by BNSF as "Regulatory micromanagement".

- **Comment:** BASF strongly believes the need for certainty in the process by the shippers, their customers, the public and the economy, i.e. the parties who will pay for any merger, far outweighs perceptions of a need for certainty in the financial markets, i.e. the only parties who might benefit if a merger fails operationally. The additional certainty provided by a successful merger should provide further assurances for the financial markets.
- **Comment:** The issue of clarity of distinctions is readily resolved in the STB process. The statutory deadline could easily be satisfied within the three-step process.

CP's comments on the proposed three-step process are much the same as those expressed by BNSF. CP describes the procedure as, "...simply expanding the number of regulatory steps required to obtain merger approval, without enhancing the ability of the STB and the public to gauge the impacts of future transactions."

- **Comment:** There is apparently a misunderstanding by these parties as to the form and purpose of the three step process and the purpose of breaking the merger process into more manageable segments. The three-step process proposed by BASF does not contain additional review or approval steps compared to procedures contained in the STB's merger regulations, as currently proposed. The three-step process places the steps for approving a merger into a logical progression in order to assure a higher degree of confidence in its success. It was not intended to prolong the time frame for Board approval and it certainly does not expand the review or approval processes.
- **Comment:** If the proposed three-step process merely increased the number of regulatory hurdles required for merger approval, we might agree with the CP. However the proposed three-step process produces substantial benefits and would materially reduce the likelihood of major merger disasters. This is particularly important as we move toward rail mergers far more complex than any previously experienced. Failing to require a systematic approach such as we recommend would be a breach of the public trust.

- **Comment:** In light of the problems that have occurred in the most recent mergers the Board, along with virtually all other interested parties, is primarily interested in improving the merger process and avoiding a repeat of the past disruptions. This is the primary purpose of the three-step procedure.

Two other issues relate to the merger process area. These are (1) the merger procedural time frame and (2) the provision of data on a transnational merger.

Procedural time frame

The STB's current time frame for a major transaction is one year after the primary application has been accepted. While most parties accept this, some offered dissenting views.

UP points out that under 49 U.S.C. §11325(b) the Board must issue a decision within 15 months after acceptance of an application. They further stress that all of this time would be required given the much larger volume and more detailed service and market data that must be reviewed in the revised process.

In opposition to UP's position, BNSF suggests that the one-year time frame commence with the pre-filing notice of a merger by the applicants.

- **Comment:** BASF recognizes the increased workload that will be placed upon the STB's staff by both the increased data that will be filed and by the sheer volume of detailed data that will be associated with the expected transcontinental mergers. BASF agrees with UP's proposal to use the maximum amount of time available to the STB in this process. BASF also agrees with the UP rationale for including this time frame in the regulations; simply put, the time will be needed.
- **Comment:** BNSF appears to be primarily concerned with reducing the time to the absolute minimum, regardless of associated risk. In addition, BNSF would start the procedural time clock when the applicants make the pre-filing notice of a merger. This would begin the procedural time frame with no substantial data available for review and analysis. In other governmental merger proceedings the clock does not start until the filing of all required information is complete. In effect, the BNSF position reintroduces BNSF's original position of limiting the time frame to 9 months, a position others, including UP, labeled as unreasonable. We believe that nine months is insufficient.
- **Comment:** Two related issues must be considered: first the overall time frame and second the starting point for the time frame. BASF has previously stated that the STB has to make perfectly clear the point at which they consider the time frame for approval has begun. This milestone sets the calendar in motion. The calendar can not be set in motion before the data needed for analysis is available.

Provision of data by non-U.S. railroads

- **Comment:** On the issue of the data that is to be provided by non-U.S. railroads involved in a transnational merger, even the Canadian railroads now agree that full system data should be provided.
- **Comment:** BASF continues to have a problem with the proposed regulations' failure to identify with any specificity the data that will be provided by non-U.S. railroads. More precisely, the data for costing purposes, statistics and accounting amounts, is not discussed in the proposed regulations. The final regulations should specify that the non-US railroads shall provide the operational and cost information in a format that is comparable to that of the US railroads involved in the merger under review. This is well within the capability of CN and CP, the two most likely non-US participants.

IV. The STB Should Address Merger-Related Service Failures Proactively.

Recent mergers of Class I railroads have led to major service problems. Not only have the railroads lost money due to these problems, numerous businesses, in effect "innocent bystanders" of the merger have sustained damage as well.

BASF and many other shippers sustained substantial damages in these mergers. And yet, they had little control over, or input into, the situation. Despite widespread service failures resulting from one major merger, subsequent mergers were allowed to follow the same failed merger procedures. Many shippers had no choice other than to devise alternative arrangements and hope for the best.

No one, including the Class I railroads, wants to repeat that experience. Another such drastic deterioration in service will be judged a major policy failure; a policy failure that was totally preventable. It was, and is, preventable by appropriate pre-merger testing. Currently there is no provision for pre-merger testing and review.

Even post merger oversight did not protect shippers from the railroads' massive "merger hangovers". BASF recommends that the Board insist on minimal service disruptions in future mergers. The policy of the STB, geared to post-approval actions, has been proven ineffective in recent complex mergers. In the next round of mergers the cost of failure will be extremely high. The STB can not afford to take a "wait and fix" approach. The Board must take steps before the actual merger to reduce the likelihood of a repeat of the major service problems encountered in previous mergers.

Comprehensive and rigorous pre-merger testing and step-wise integration of systems is required if service disruptions are to be avoided or at least contained and curtailed. BASF has recommended this type of testing and integration as part of the three-step merger approval process. The Blue Ribbon Advisory Panel we recommend would be a logical entity to have review and approval of each step as one of its areas of responsibility. Failure to require and conduct pre-merger testing, with persuasive

indications that the various aspects of the individual systems will mesh, makes a repetition of past trauma almost inevitable.

Merger applicants are required to identify potential problem areas prior to the actual merger. Not only should the merger applicants identify these potential problems, they should be required to implement means to prevent the problem before it compounds and spreads. Additionally, as part of their merger application, the applicants should be required to obtain a written commitment from the other railroads, including involved short lines, on the assistance they will provide in the event of merger-related service problems. A proposed plan, with no such written agreements, is not enough.

The short line railroads have proven to be versatile and valued links in the supply chain. BASF sees them as a vital part of the solution. Not only have they proved invaluable during service crises, routine operations have also benefited from their involvement. Careful examination of the impacts of mergers on small railroads and development of appropriate protection for these vital links in the supply chain is important in maintaining service. We urge the STB to support and expand the short lines' role in the merger process.

While a positive change in the Board's merger policy will go far towards minimizing the chance of severe service disruptions, the railroads must nevertheless be held accountable for their actions. Many respondents, including BASF, have called for service guarantees. The railroads should be willing, and in fact required, to comply.

Moreover, the timing and urgency of the remedy should not be left to the operating convenience of the railroads. Time is of the essence in restoring service. Bitter experience in past mergers has shown that problems can compound and multiply quickly. Both the railroads, the shippers and their customers deserve prompt, effective and targeted response when service problems arise. The remedies should be timely and low cost. The two concepts are related. Rapid response will often catch the problem before it grows to unmanageable and expensive proportions.

The service guarantees should be reasonable - providing relief economically and efficiently before service disruptions threaten the operating and financial health of the shippers, and the railroads themselves

BASF recommends a two-pronged approach to compensation. First, as a temporary remedy, shippers damaged by deteriorated service and other merger problems should be compensated in monetary terms for the losses sustained. In our previous filings we have outlined limited monetary damages consisting of the railroad paying the cost of car leases caused by service failures. We also outlined more extensive monetary damages for plant curtailments and shutdowns caused by railroad service failures. Second, the lasting remedy is restoration of service to pre-merger or better standards. Monetary damages are not sufficient to recoup the losses sustained by shippers during a merger-related service collapse. The real and lasting remedy is restoration of service.

"Service damage" bills rightly assign financial responsibility for the service failure to the railroad(s) causing that failure. The applicants will no doubt oppose such costs. However, these types of monetary damages amount to only a small portion of the full damages sustained by shippers due to merger-related service failures.

While the shippers should be compensated for merger-related service failures, the railroads should be protected from frivolous claims, claims not truly related to the merger at hand.

The Board should establish rules and procedures for the prompt resolution of merger-related service complaints. The rules would prescribe procedures for the filing of complaints, establish appropriate investigative and adjudicatory entities, and set forth the basis for compensation to aggrieved shippers. The Blue Ribbon Advisory Panel could have a role in establishing these rules and procedures.

Discussion of Alternative Views

Service Failures

The issue of merger-related service failures is recognized by the railroad industry as well as by shippers and other users of rail service as one of the most important aspects of the merger process, and one of the most dangerous. In their reply statements several railroads commented on this issue.

CSX stated that the Board "...should impose rigorous planning requirements to ensure that operational integration issues are formally addressed, and should closely monitor the operational progress of integration." They further stated that the railroad is in the best position to identify service problems and it would be premature for the STB to determine every detail of operational monitoring data that should be required. Finally, CSX noted that the specific set of data proposed in §1180.1(c) is not all-inclusive, and does not preclude the use of other information.

NS noted as a constructive measure the requirement to develop a service assurance plan (SAP). The SAP is intended to minimize or eliminate service disruptions and provide a process of operational monitoring to respond to service problems that might arise. Finally, NS stated that it is essential that the Board retain flexibility in its operational monitoring requirements.

It appears that NS and others believe that developing the Service Assurance Plan (SAP) and other rigorous planning will eliminate the service failures experienced in recent mergers. Not so.

- **Comment:** Despite the fact that the railroads involved in recent mergers claimed they had done everything they believed necessary to operate the combined systems on a near normal basis, the result was massive service failure. Despite the fact that the planning by the involved railroads was claimed to be extensive, including a massive effort by their personnel and coordination with shippers through the

Transaction Council, the result was massive service failure. In two major mergers the end result was service failure, despite their best efforts. CSX correctly pointed out the rigorous planning required, indirectly highlighting the inadequacy of the BNSF nine-month timeframe.

- **Comment:** CSX's statement that the railroads are in the best position to identify service problems is not completely true. It is necessary to recognize the signs of an impending failure, and then move rapidly to prevent or remediate the problem. Only with recognition of the problem is it possible to apply an appropriate preventative measure or remedy. Shippers can assist in problem recognition. It is well to remember that for months UP experienced operational delays, which they were reluctant to acknowledge. The problems multiplied and spread to impact the UP system, connecting roads, and customers. BASF submits that it would be much more effective to involve shippers and others such as the Advisory Panel in the identification of the problem and the application of solutions.
- **Comment:** BASF believes that developing the Service Assurance Plan (SAP) is only part of the solution. The review and analysis of outside parties such as the Advisory Council and the Board's own staff are an integral part of averting a repeat of the past service failures. The consequences would be catastrophic if the UP/SP or CSX-NSC-CR situations were to occur in a transcontinental merger.

The railroads viewed operational benchmarks as flexible and subject to redefinition with each merger.

- **Comment:** BASF stated previously in its filings in this proceeding that pre-merger benchmarks are a critical element and an early indicator of potential service failures. While their definition may be flexible to some degree, basic measurements apply to operational areas on a consistent basis. For example, dwell time for all major classification and interchange yards should be computed in a pre-merger environment as well as the transit time and/or train speed over primary traffic corridors that connect major transportation centers. The types of data collected in the UP/SP monitoring process offer a good starting point for consideration. Failure to collect specific data in a pre-merger operating environment causes much of its value to be lost.

Compensation for Shippers

With regard to compensation to shippers for service related failures, UP, NS, and BNSF offered comments. UP's position is that negotiating service agreements can play a useful role in protecting shippers against service failures.

NS states that the proposal to have the Board administer claims proceedings should be rejected. They further state that shippers can use the normal venues to seek redress, such as the courts.

BNSF takes the position that the procedures for resolving disputes should be based on the formulation proposed by DOT. The remedies in this proposal include access to alternate transportation, rate discounts or recovery of losses. These should be developed specifically within the individual merger.

- **Comment:** UP's suggestion that the compensation issue can be worked out in service agreements would be correct if the railroads would guarantee effective service standards in their service contracts. However, in contract negotiations the railroads are very reluctant to include meaningful service guarantees especially if coupled with monetary penalties. The idea is good in theory but wanting in practice. In addition, shipments moving under tariff rates would not be afforded any protection.
- **Comment:** The BNSF proposal, based on the DOT concept, is also a good procedure but may be limited in application. Access to alternate transportation can have two applications, (1) intramodal and (2) intermodal. Access to another railroad is not always possible since many shippers are only served by one railroad and the mechanics of getting another railroad to the shippers facility is often not feasible. As for intermodal, the availability of this option depends on whether the shipper had loading facilities for the alternative mode and whether or not the receiver has facilities for handling the alternative transportation mode. For some products, there simply is no realistic alternative mode option. We see certainty of damage paired with faint possibility of remedy.
- **Comment:** Compensation for losses is an issue that BASF addressed in its previous statements in this proceeding. The NS remedy with rail shippers using the courts to seek damages really says the status quo is adequate. We and many others see it differently. The Board is attempting to make the revised merger regulations as comprehensive as possible with regard to the key issues. Financial damage to a rail user resulting from merger-related service failures is a key issue. It can be and should be remedied within the regulations that govern the merger process.

V. The Board Should Not Only Protect Competition, It Should Enhance It.

At this advanced stage of the railroad merger process, with end-to-end mergers expected, we see limited improvements to competition from rail mergers. We also see possible losses in the choice of connecting carrier on east-west movements. Accordingly, the need to enhance competition is increasingly clear. The STB recognizes this. Future mergers must not only not threaten competition, they should enhance it as well. The previous merger review provisions have accomplished their intended purpose of increasing efficiency and reducing excess capacity. They have now outlived their usefulness. BASF and the other participants in this proceeding have offered simple and effective remedies for accomplishing this most important goal.

Preserving Competition

BASF recommends implementation of a strong pro-competitive policy. As we have suggested, the rules should include an explicit requirement for the applicants to identify with specificity each and every significant instance of reduced competition, with a concomitant requirement to propose a specific practical and effective remedy for each such situation. This will protect individual shippers from the loss of competitive alternatives stemming from the merger of Class I railroads. This provision will also force the railroads to develop creative solutions to the anti-competitive aspects of their consolidations.

While the applicant railroads should be required to provide competitive solutions and enhancements, they should not have a monopoly on this. Typically in such situations the parties have little incentive to offer anything but the minimum they believe necessary to secure approval of their application.

Shippers and other non-applicants are well equipped and, more importantly, well motivated to identify potential harms and appropriate remedies. BASF recommends that shippers, Class II and III railroads, the recommended Advisory Panel and other affected parties be afforded equal status with the applicants when it comes to identifying competitive harms and recommending strategies to prevent them, as well as providing suggestions for enhancing competition. The regulations should be modified to allow and encourage this. The STB should mandate consideration of that input by requiring a revised applicant railroad mitigation plan, reflecting shipper and non-applicant input.

Vice Chairman Burkes is correct in his belief that rail-to-rail competition is what is lost in mergers. However, most of the rail to rail intramodal competition between Class I railroads is now in the past, already lost. Precious little rail to rail competition remains to preserve. Concomitantly, one can question how much rail-to-rail competition will be affected by the next round of mergers, except at the gateways. The focus shifts from preserving rail competition to enhancing rail competition. Haulage rights, trackage rights and reciprocal switching are just some of the proven means of enhancing rail competition.

Enhancing Competition

Throughout this proceeding, BASF and many other respondents have recommended limited open access procedures for enhancing competition such as reciprocal switching, "interswitching," shared asset areas, competitive line rates, haulage and trackage rights, and other pro-competitive measures.

Permitting shippers to challenge bottleneck rates, regardless of the makeup of the through rate, was widely recommended by many respondents. Currently, a shipper seeking relief from exorbitant rates for route segments that are totally captive to a single carrier now faces virtually insurmountable obstacles. The Board's policy should be changed to correct this. A change in Board policy to acknowledge such shipper grievances would be a major improvement in the effectiveness of the competitive rail market. Such change coincides with a broad policy shift toward greater

competitiveness and shipper empowerment. Challengeable rates will lead to competitive rates – and enhanced competition is the Board's stated goal.

The simplified rate reasonableness challenge could also be extended to maximum rate cases. The Blue Ribbon Advisory Panel can assist in developing simplified and more accessible procedures. Such simplified procedures can also make it less expensive to challenge rates. Currently, the cost of a rate reasonableness test is itself unreasonable and disenfranchises most shippers from seeking a regulatory remedy. The current procedures present a major impediment to regulatory access except for those parties with the persistence and financial resources to pursue the seemingly interminable and frequently fruitless pathway of maximum rate challenges.

BASF and the other participants in this proceeding have offered simple and effective remedies for this and other serious problems surrounding rail mergers.

While the Board's proposed rules require the applicant railroads to propose strategies for enhancing competition, these proposals will be constrained by the fact that only the merging systems can offer the concessions that might increase shipper choice. The merging railroads have no power to recommend solutions that would affect non-merging lines, other than to permit them greater access to their own customers. While such proposals may enhance competition, they are unlikely to occur since they result in the merging railroads offering all the concessions, and the non-merging lines offering none.

For this reason, BASF recommends that the Board convene independent inquiries at the time it examines the next merger to consider industry-wide reforms that would enhance competition broadly, not just within the context of the merging railroads. These reforms would deal with rights of access, reciprocal switching zones, competitive rate plans, and the rights of shippers to appeal against unreasonable rates and terms of service.

Discussion of Alternative Views

Preserving and enhancing competition is, as might be expected, a polarizing issue for many railroads and rail users. CSX, UP, NS, BNSF, CP and CN all take the position that enhancing competition in situations that are not related to the merger application under review is wrong. The railroads have characterized enhancing competition as, reregulation, disguised open access, and a lead-in to a return to the inefficiencies and other problems that plagued the industry pre-Staggers Act.

Additionally, CSX and BNSF discussed the vague nature in which this issue was included in the Board's proposed regulations. BNSF even added that they "lacked standards". In further justifying the exclusion of non-merger-related competitive enhancements both CSX and UP stated that this approach conflicts with the merger policy employed by the Board and the ICC in past mergers. CSX stretches the record in stating that, "...requiring 'unrelated competitive enhancements' has garnered essentially no support among commenting shippers...".

- **Comment:** Characterizing the Board's inclusion of the concept of enhanced competition as reregulation, a return to the pre-Staggers Act inefficient railroad industry, and a disguise for open access can only be seen as scare tactics. The argument that this was not the policy embraced by the ICC or the Board in past mergers is in part reflecting the change in thinking on the agency's part regarding the competitive situation that currently exists with regard to users of rail service.
- **Comment:** The railroads surely recognize that for years the ICC/STB merger policy has required balancing of the public interest and the railroad's corporate interest. The current lack of rail alternatives is in large part the direct result of past mergers. This rather suggests that the ICC/STB balancing of interests tilted too far against the public interest. This proceeding is intended to correct that imbalance. Simply put, the competition issue was not dealt with in a manner that recognized the accumulation of monopoly power that would occur with successive mergers.
- **Comment:** The statement by CSX that the concept of competitive enhancements had no support among shippers misstates and misrepresents the extensive shipper filings. The CSX claim that shippers are not in favor of enhancing rail competition is blatantly incorrect. As pointed out by BNSF the inclusion of competitive enhancements in the proposed regulations is vague and lacks standards. While some shippers may have a problem with the issue, as it is currently included in the regulations, there is virtually no shipper opposition to the concept of enhanced competition. BASF, like many shippers, proposed several proven procedures that can be used to enhance rail competition and noted that the resulting open access is to be limited in scope and application. The Board must supply specifics as to the framework under which this concept will be put into action. CSX's claims notwithstanding, enhancing rail competition has wide and solid shipper support.

Another aspect of the enhancement of competition relates to the issue of bottleneck rates. CSX, UP and NS offered comments on this issue. CSX proposes that the Board continue to limit the bottleneck exception to situations where there are existing contracts, otherwise it is characterized as reregulation. UP states that the merging railroads make available separately challengeable bottleneck rates between exclusively served facilities on their system and the predominant pre-merger gateway. NS agrees with the Board's proposed rules, which preserve the opportunity to enter into contracts on one segment of the movement in order to gain relief for the remainder of the movement.

- **Comment:** BASF adheres to its position that any portion of the rate should be open to challenge and should stand on its own merits. The UP railroad also did not support requiring the inclusion of the contract provision as a pre-condition to challenge bottleneck rates. While BASF applauds UP's approach it is limited to pre-merger predominant gateways. Broader application is required.

The final issue for discussion in this section is gateways. The railroads appear to be fearful that some parties are asking for a return of the DTI conditions with regard to gateways. CSX, UP, NS and BNSF all commented on limiting the retention of gateways in a post-merger environment to those they characterize as efficient, economic, major or important.

- **Comment:** BASF agrees that only major gateways that are currently being used in the movement of rail transportation should be considered in satisfying this requirement of the merger regulations. BASF does not advocate a return to the DTI conditions regarding the gateway issue in merger proceedings. Opening gateways that meet the efficient, economic, major or important criteria provided by the railroads above will enhance the efficiency of the national rail transportation and should be required by the Board.

D. Conclusion

The remedy is clear. The STB should require specific actions by the railroads centered on rigorous pre-merger testing and step-wise integration of systems within a 3-step merger approval process. An Advisory Panel responsive to the Secretary of Transportation and empowered to deal with specific technical areas should be created to assist during the merger process.

The key areas identified by BASF are:

- **The Critical Need for Enhanced Competition**
- **Open Gateways and Limited Open Access**
- **Challengeable Bottleneck Rates**
- **Implementation Plan and Merger Oversight**

In each of these areas the need and the remedy are clear. The numerous respondents supporting changes similar to those recommended by BASF reinforce the clarity of both the need and the remedies. Exhibit A summarizes the widespread support for change in these four key areas.

The remedies presented by BASF can help reverse the adverse rail performance trends and should be adopted by the Board.

In summary the recommended initiatives include:

- **Actions that implement the STB policy decision to enhance competition**
- **Adoption of a 3-step merger review and approval process**
- **Procedures to prevent and recover economic losses caused by service failures**

- **A stronger rail merger implementation and oversight role for the Secretary of Transportation, including an empowered Advisory Panel reporting to the Secretary of Transportation**

As noted in the Comments, history shows clearly that problems caused by monopolistic practices led to legislative remedies, including the Interstate Commerce Act in 1887. Prolonged regulation left the rail industry in weakened condition and led to the Staggers Act, which deregulated the rail industry in 1980.

Now, with rail to rail competition reduced or eliminated by mergers, there is a danger that the railroads are regressing toward monopolistic practices. The STB has the duty and the responsibility to ensure through fair and equitable merger guidelines that the path goes forward. Failure to do this can lead to a replay of history culminating in draconian legislative remedies; an outcome no participants want.

Exhibit A: Summary of Recommendations of Other Parties¹**• Open Gateways**

The following parties agreed with key elements of our **Open Gateways** proposal:

Canadian Pulp & Paper
CMA
CSX
• only applies this principle to "traditional" gateways
Dow
DuPont
Glass Producers Transportation Council
NITL
PPG
PPL Montana
Proctor & Gamble
Shell
Society of Plastics Industry
UP
• only applies this principle to "traditional" gateways
USDA
• also discusses opening previously closed gateways
USDOT

• Competitive Access

The following parties agreed with key elements of our **Competitive Access** proposal:

Alliance for Rail Competition
American Shortline and Regional Railroads
Canadian Pulp & Paper
Canadian Resource Shippers Corp.
CMA/APC
Consumers United for Rail Equity
Dow
DuPont
Farmrail
Glass Producers Transportation Council
MRL
MRL, I&MRL
National Association of Port Authorities
NITL
Ohio Rail Development Commission
Ports of Seattle, Tacoma, Everett
PPG
PPL Montana
Proctor & Gamble
Shell
Society of Plastics Industry
USDA
USDOT
Western Coal Traffic League
Weyerhaeuser

¹ Reflects filings through November 17.

<ul style="list-style-type: none">• Bottleneck Rates

The following parties agreed with key elements of our
Revision of Bottleneck Rates
proposal:

Alliant Energy Corporation
Canadian Pulp & Paper
CMA/APC
Consumers Energy Company
Consumers United For Rail
Equity
DOW
DuPont
Glass Producers Transportation
Council
NITL
Ohio Rail Development
Commission
PPG
PPL Montana
Procter & Gamble
Society of Plastics Industry
UP
USDOT
Western Coal Traffic League

<ul style="list-style-type: none">• Implementation Plan
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The following parties agreed with key elements of our proposal calling for a
**Detailed Implementation Plan with
Merger Oversight Mechanisms:**

Amtrak
California Attorney General
California Public Utilities
Commission
Canadian Pulp & Paper
CMA/APC
CSX
• lacks mention of benchmarks
and real-time simulation
DME
DuPont
Finger Lakes Railway Corp.
GM
Iowa DOT
National Mining Association
NITL
Port Authority of NY & NJ
PPG
Society of Plastics Industry
State of NY
UP
US Clay Producers
USDOT

Economic and Management Consultants

Tom O'Connor: Experience
Snavely King Majoros O'Connor & Lee,
Vice President (1988-Present)

Mr. O'Connor has more than twenty-five years experience in the transportation industry. His experience includes key and increasingly responsible management and policy positions with government agencies and private industry.

Mr. O'Connor, in recent years has conducted analyses for the Government of Canada used to shape policy for freight transportation transport policy. He also has developed the Master Plan for Management Information Systems and computer facilities to measure, manage and monitor both rail freight and rail passenger transportation for the Bulgarian State Railways, in Bulgaria and the Balkan Peninsula. He has created and managed numerous computerized transport management and regulatory systems and is a widely recognized expert on costing and economics.

Mr. O'Connor has analyzed more than 45 rail merger scenarios and cases. He has provided expert testimony before state and federal courts and commissions in the U.S. and Canada on economic and policy issues. He has also testified as an expert on computerized transportation analytical systems, rail operations, anti trust issues and transportation costing. Mr. O'Connor also has served as an impartial and expert monitor of data and processes at issue in litigation on transportation.

Within the litigation arena, Mr. O'Connor has also conducted management audits of railroads, focused on identifying the cause and effect relationships underlying claimed cost incidence. The management audits were directed toward testing the cost basis of bills submitted by major railroads.

DNS Associates Inc.,
Vice President (1982 - 1988)

Mr. O'Connor directed and participated in numerous projects including merger analyses, transportation infrastructure analyses, plant and network rationalization and feasibility studies. He designed and implemented mainframe and microcomputerized systems for analyzing rail,

truck and barge logistics. The computerized cost systems Mr. O'Connor created are in widespread use throughout the United States and Canada.

Mr. O'Connor also advised the U.S. Rail Accounting Principles Board on the costing aspects of regulatory reform policies. He also provided expert testimony on computerized data bases and cost systems and related rail cost issues before the Interstate Commerce Commission.

Association of American Railroads,
Assistant Vice President, Economics
(1979 - 1982)

Mr. O'Connor designed and managed major economic analysis projects. He helped formulate industry economic policy positions culminating in the Staggers Rail Act of 1980. He submitted expert testimony on behalf of the railroad industry in numerous cases before the Interstate Commerce Commission and state regulatory commissions. He also appeared regularly in national forums on economic issues.

Mr. O'Connor directed the most significant computerized industry Costing System project in 40 years, URCS, the cost system now used by all major US railroads. He also conducted industry seminars on URCS and related economic issues. Mr. O'Connor also testified before the Interstate Commerce Commission on the design and application of this pathbreaking rail cost system since adopted by the Commission and the rail industry.

He also directed development and installation of a commercial computerized economic and market analysis system now used by virtually all major US railroads.

Consolidated Rail Corporation,
Assistant Director, Cost & Economics
(1977 - 1979)

Mr. O'Connor was responsible for all Conrail management and regulatory cost analyses in both freight and passenger areas. He testified before the ICC on the development of subsidy standards now widely used in the US railroad industry. He also finalized the design, and implemented and managed Contribution

Economic and Management Consultants

Simulator and Calculator (COSAC), a computerized internal management economic analysis system at Conrail. The COSAC system uses specific management accounting data to develop economic costs. COSAC replaced earlier systems and was used to guide virtually all transportation management decisions.

Mr. O'Connor also participated in cost allocation negotiations between Amtrak and Conrail on cost sharing of joint facilities on the Northeast corridor. He initiated and directed profit maximization and plant rationalization programs. He also designed and implemented computerization and improvement of a wide range of economic and cost analysis systems used to manage this multi-billion dollar corporation.

**R.L. Banks & Associates Inc.,
Consultant (1976 - 1977)**

Mr. O'Connor conducted and directed numerous transportation-related projects in the U.S. and Canada ranging from national logistics analyses to site-specific studies. He specialized in costing systems and appeared as an expert witness on such systems in a precedent setting proceeding before a Canadian Crown Commission.

**U.S. Railway Association,
Manager, Local Rail Service Planning
(1974 - 1976)**

Mr. O'Connor developed, computerized and implemented the light density lines cost analysis system, which defined Conrail. He served as liaison with congressional staffs and shipper groups, as well as federal, state, and local governments, and planning agencies. The system he created was a major element in the design and implementation of the streamlined Midwest-Northeast regional rail system. Mr. O'Connor subsequently appeared as an expert witness to present and defend the operation of the USRA costing system.

**Interstate Commerce Commission,
Economist, (1973-1974)**

Mr. O'Connor served as a staff economist and authored a report analyzing industry investment patterns and ICC regulatory policy, including ICC use of cost evidence.

Education

- University of Massachusetts, Amherst, B.A. Economics
- University of Wisconsin, Graduate Course Work, Economics
- University of Delaware, Graduate Course Work, Business Management
- The American University, Graduate Course Work, Computer Science

Professional Organizations

Transportation Research Board

- Former Chairman Surface Freight Transportation Regulation Committee

Transportation Research Forum

- Former President of the Cost Analysis Chapter

National Defense Transportation Association

- Member of Board of Directors, National Capital Chapter

Phi Beta Kappa academic honors society

Phi Kappa Phi academic honors society

Military

U.S. Army; Sergeant, Combat Engineers

Security Clearance

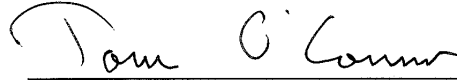
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SK Snively King Majoros O'Connor & Lee

Economic and Management Consultants

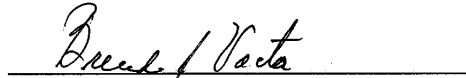
VERIFICATION

I, Tom O'Connor, declare under penalty of perjury that the foregoing statement is true and correct and was prepared by me or at my direction. Further, I certify that I am qualified and authorized to file this statement. Executed on January 11, 2001.



Tom O'Connor

Subscribed and sworn to before me this 8 th day of January 2001 in the District of Columbia.




Notary Public

My Commission expires 6/3/2003

Notice of Service

Copies of this Verified Statement and the accompanying Comments were served by first class mail on the Parties of Record for Ex Parte 582 (Sub No.-1).



Tom O'Connor

January 11, 2001

Ex Parte No. 582 (Sub-No. 1)